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Tax Planning for Severance Packages

Over the past year, economic stresses worldwide have resulted in many employees receiving severance packages and being advised that their services are no longer required. The longer you've been employed with an organization, the higher your severance package will be. With the national job market still experiencing varying levels of stress, it is more important than ever to hang on to as much money from an employment severance settlement as possible.

If you don't plan ahead, the tax authorities have no problem relieving you of your extra money. A professional tax and investment advisor will run through the options with you and help you choose a strategy that best fits your circumstances.

Tax Shelter Strategies For Severance Pay

Registered Retirement Savings Plans (RRSP)

Most of us are aware of the tax advantages of RRSPs. If you've been following your financial planner's advice, you've been socking away as much money into your retirement fund as possible. Assuming you have room to invest, placing your severance pay into an RRSP is an ideal investment option. Spousal RRSPs, income splitting, and maximizing foreign content are all options to discuss with your tax advisor.

That's the easy part. As mentioned earlier, the job market is less than ideal. If you find yourself needing those funds at a later date for living expenses, it is best to contact a financial professional. They will review your situation and provide you with the best option for managing your tax burden while protecting your investment and providing you with funds.

Retiring Allowance

This investment option allows you to shelter severance pay based on the duration of service with the company and the particular years employed. The amounts that can be transferred vary depending on the years you were employed. Due to the complexity of the calculation, a tax and investment planner will be able to advise you on its merits. The retiring allowance can be used over and above the limits imposed upon RRSPs.

Tax Sheltered Insurance Accounts

A tax sheltered insurance account allows you to acquire tax-free earnings within the policy. It can provide for future retirement income at a reduced tax rate and offers tax-free proceeds to your estate. This may not be the best option for investing your severance package; however, if other options are maxed out, you may want to discuss this with your financial advisor.

Invest Your Severance Pay into Your Own Business

You likely don't want to invest your severance directly into a business opportunity as Canada Revenue Agency will be looking for 30% or so off the top. You can, however, shelter the money and then withdraw funds as you need them. Your tax burden will be reduced due to the fact that your income is lower during the start-up period. When jobs are scarce, starting a new business is often a viable option for those who have been downsized. Before starting any new enterprise, consult with a tax professional to learn all about the best tax planning ideas for entrepreneurs.

If you have Tax Planning questions, be sure to let us know by phone or email!

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